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IN THE

Supreme Court of the United States

..... TERM, 1962

No. 916

IN THE MATTER OF THE APPLICATION OF

PERCY C. and MARGARET A. MAGNUS

to quash certain summonses issued by the Internal Revenue Service to testify, and produce records, etc.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

TO THE HONORABLE CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

The petitioners pray that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit affirming the order of the United States District Court for the Southern District of New York.

Opinions Below

The opinion of the United States District Court for the Southern District of New York (App. 18a)* is reported at

* Parenthetical references are to the appendix in the Court of Appeals.

196 F. Supp. 127 (S.D.N.Y. 1961). The opinion of the United States Court of Appeals for the Second Circuit, decided February 13, 1962, has not yet been reported but is reproduced in the Appendix hereto beginning at page 20.

Jurisdiction

The appeal to the Court of Appeals for the Second Circuit was decided February 13, 1962. A petition for rehearing and a petition for rehearing *en banc* were denied, and the mandate issued to the United States District Court for the Southern District of New York on March 27, 1962. The jurisdiction of this Court is invoked under Title 28, U.S.C., Section 1254(1).

Questions Presented

1. Whether the decision of the United States Court of Appeals for the Second Circuit, which directly conflicts with the holding of the United States Court of Appeals for the Ninth Circuit on the statutory construction of Section 7605(b), I.R.C. 1954, and which affirms the summary denial by the United States District Court for the Southern District of New York of petitioners' application to quash summonses issued by the Internal Revenue Service upon third parties allegedly having knowledge of and in possession of documents relating to the criminal tax liability of the petitioners under investigation, was error.

2. Whether the summary denial of petitioners' application for a hearing to ascertain whether a third investigation by Special Agents of the Internal Revenue Service should be classified as "unnecessary" within the purview of Section 7605(b), I.R.C. 1954 was an erroneous denial of petitioners' right to due process of law under the Fifth Amendment of the Constitution and Section 7605(b), I.R.C. 1954.

3. Whether an attempted enforced examination, inspection and production of the records of the petitioners' accountant and the records of a corporate employer relative to their personal tax liability for the years in question fall within the meaning of the words "* * * examination or investigations * * *" as they appear in Section 7605(b), I.R.C. 1954.

4. Whether the United States Court of Appeals for the Second Circuit was in error in holding that "* * * examination or investigations * * *" within the prohibitory purview of §7605(b), I.R.C. 1954, occur only when it is the taxpayer directly or records in his possession which are examined, and not when the taxpayer is examined, or investigated by and through testimony and records in the possession of his accountant and corporate employer.

5. Whether the holding of the Court of Appeals that, as a matter of law, Internal Revenue Service summonses directed to an accountant and to a corporate employer, encaptioned "In the Matter of the tax liability of Percy C. and Margaret A. Magnus" was an examination of the persons summoned and *not* an "examination or investigation" of the captioned taxpayers, was error.

6. Whether the decision of the United States Court of Appeals for the Second Circuit, excluding from the purview of §7605(b), I.R.C. 1954, investigations conducted through third parties, rendered a nullity the prohibitions and protections provided for by Congress in that section as a check upon the summary investigatory powers of the Internal Revenue Service.

7. Whether, in a proceeding to quash Internal Revenue Service summonses issued to third parties allegedly having knowledge of and possession of records pertaining to a taxpayer's personal tax liability under criminal investigation, the United States District Court for the Southern

District of New York violated the taxpayers' statutory rights under § 7605(b), I.R.C. 1954, and the Fourth, Fifth and Sixth Amendments of the Constitution by reaching a determination as to the factual issue necessarily raised and in dispute under § 7605(b), solely upon consideration of affidavits presented and not upon testimony duly taken at a hearing and subject to the test of cross-examination.

8. Whether the taxpayers-petitioners were deprived of their right of cross-examination and confrontation of witnesses under the Fifth and Sixth Amendments of the Constitution when the United States District Court for the Southern District of New York refused to grant a hearing of any nature whatsoever on the propriety of the issuance of Internal Revenue Service summonses which were an unnecessary part of a criminal investigation for an alleged violation of the Internal Revenue Laws of the United States.

Statute Involved

26 U.S.C. § 7605.

"(a) • • •

(b) **Restrictions on examination of taxpayer.**—No taxpayer shall be subjected to unnecessary examination or investigations, and only one inspection of a taxpayer's books of account shall be made for each taxable year unless the taxpayer requests otherwise or unless the Secretary or his delegate, after investigation, notifies the taxpayer in writing that an additional inspection is necessary. Aug. 16, 1954, 9:45 A.M., E.D.T., c. 736, 68A Stat. 902." 26 U.S.C. § 7605.

Statement

This is a petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit, arising out of an affirmance by that Court of an order of the United

States District Court for the Southern District of New York denying petitioners' application and motion for an order, pursuant to Title 26, U.S.C., § 7605(b), quashing summonses issued by the Internal Revenue Service pursuant to Title 26, U.S.C., § 7602, requiring Hurdman & Cranstoun, Certified Public Accountants of New York City, and Magnus, Mabee & Reynard, Inc., of which company taxpayer Percy C. Magnus is president, director and stockholder, to produce records, etc., and to testify before a Special Agent of the Internal Revenue Service.

The accounting services of Hurdman & Cranstoun have been utilized both by the taxpayers and by Magnus, Mabee & Reynard, Inc.

This petition also relates to the denial of a hearing below on the foregoing application whereby petitioners were deprived of the opportunity to present evidence and challenge that presented by the government at an adversary proceeding where the issues necessarily raised by the petitioners' claim of protection from a third investigation, pursuant to § 7605(b), I.R.C. 1954, could be properly and equitably considered by the Court. The summonses which the taxpayers under criminal investigation are seeking to quash required the above-mentioned companies to appear before George Akkerman, a Special Agent of the Internal Revenue Service, on June 30, 1961. Compliance with the summonses has been stayed pending disposition of the pending petition for certiorari.

In the year 1959, petitioners were the object of an Internal Revenue Service investigation conducted by the office of the Special Agent in charge in New York. The criminal investigation then being conducted had as its subject matter the alleged late filing of tax returns and was conducted by Victor Biskup, Special Agent of the Internal Revenue Service. Petitioners and their representatives extended absolute and complete cooperation, and indeed taxpayer was interviewed by the Special Agent, and his books, records, etc. were freely made available on re-

quest. Special Agent Biskup accepted petitioners' cooperation (App. 4a). This investigation terminated in 1959 with a finding favorable to the taxpayers. It is alleged, and in fact has not been denied by the government, that Special Agent Biskup determined that the evidence did not support a finding justifying a possible charge of wilfulness; and this finding was undeniably embodied in a written report (App. 5a).

The matter remained closed until the summer of 1960, when Joseph P. Gillespie, another Special Agent of the Internal Revenue Service, advised the taxpayers and their legal representatives that a new investigation relating to the same years as were covered by Special Agent Biskup, and having the same subject matter, would be initiated. Although disturbed by this extraordinary turn of events, taxpayers freely and voluntarily again extended full cooperation to the Special Agent in his investigation. As was the case with Special Agent Biskup, Special Agent Gillespie accepted the cooperation of the taxpayers and, similarly as his predecessor had done, Special Agent Gillespie interrogated the taxpayer, Percy C. Magnus, and had access to his books, records, etc. (App. 5a).

In December 1960, taxpayers were informed, through their accountants, that the Special Agent had made a finding that there was an absence of wilfulness, that the second investigation had terminated in their favor, and that, pursuant to normal procedure, the case had been referred back to the audit division of the Internal Revenue Service (App. 5a). It is undenied that Special Agent Gillespie embodied his finding that there was an absence of wilfulness in a written report.

The matter was closed until May 24, 1961, when the taxpayers were advised through their representatives that still a third Special Agent of the Internal Revenue Service, one George Alderman, had called on them and informed them that he had been requested by his superiors to institute yet another investigation of the same taxpayers

relating to the same subject matter and the same years as the two prior investigations (App. 6a).

In furtherance of this third investigation, the summonses sought to be quashed below, requiring the production of books and records designated therein, were served. The summonses sought to be quashed, copies of which were attached to the moving papers below (App. 9a, 11a) were subscribed by George Alderman, Special Agent of the Internal Revenue Service, and required the appearance of Magnus, Mabee & Reynard, Inc., Hurdman & Cranstoun, and others to appear before him on June 30, 1961 "to give testimony relating to the tax liability * * * of the above named person (petitioners) * * * and to bring with you and produce for examination the following books, records, and papers * * *" relating to the tax liability of Percy C. and Margaret A. Magnus, petitioners, for the taxable years 1948 through 1957, inclusive (App. 9a, 11a).

This third investigation of the taxpayers' affairs for the same taxable years is *prima facie* forbidden by § 7605(b), I.R.C. 1954; and, therefore, constituted unlawful action on the part of the Internal Revenue Service. That statute forbids unnecessary examinations or investigations into a taxpayer's affairs.

The proceeding below was brought on to prevent this third unnecessary and unwarranted investigation of the affairs of the same taxpayers for the same taxable years. The United States District Court for the Southern District of New York summarily, and without a hearing on the issues of fact necessarily raised by the application under § 7605(b), denied petitioners' application.

It is petitioners' position that but for the erroneous construction of § 7605(b), the application below would have been granted, because of the failure of the Internal Revenue Service to state a defense at law. Alternatively, issues of fact were raised by both petitioners' and respondent's papers, and a hearing should have been held to decide these disputed issues of fact.

Accordingly, petitioners seek reversal of the order of the District Court for the Southern District of New York, dated July 28, 1961, and direction of the entry of an order by said Court quashing the summonses in question and permanently staying the Internal Revenue Service from conducting any further investigation in reference to petitioners for the taxable years 1948-1957, inclusive. Petitioners request, in the alternative, that the said order be reversed and the case remanded to the District Court for a hearing to determine the issues of fact raised by the application made therein, which application was improperly and erroneously refused by the District Court.

The decision of the Court of Appeals for the Second Circuit conflicts with a decision of the Ninth Circuit. Such conflict engenders a lack of uniformity in Internal Revenue procedures affecting vital personal rights of taxpayers causing the existence and protection of same to depend on geographical happenstance. Under the present state of the law a New Yorker with whom a taxpayer does business may be compelled to comply with a summons in an unnecessary investigation of the taxpayer while a Californian with whom he does business may not be so compelled.

REASONS FOR GRANTING THE WRIT

POINT I

The construction below of 26 U.S.C. § 7605(b) which precluded its application to any inquiry other than one made directly to the taxpayer is contrary to plain meaning of the statute, contrary to the Congressional intent disclosed by Congressional history, and in conflict with the construction by the Ninth Circuit.

The substance of the decision of the Court below is that the relevant portion of 26 U.S.C. § 7605(b) confers a statutory right available to taxpayers, only when it is the tax-

payer himself who is summoned for an examination or investigation, and not when the taxpayer is examined or investigated by and through testimony and records pertaining to the taxpayer's personal liability, in the possession of third parties. This overlooks use of the word "examination" and the word "investigations" and represents a tortured use of both the words by giving them the same meaning, one so narrowly confined as to violate the rule of plain meaning and the intent of Congress. The pertinent portion of Section 7605(b) states as follows:

> "No taxpayer shall be subjected to unnecessary examination or investigations * * *."

The Court below takes the overly restrictive approach that Congress, in enacting the predecessor of § 7605(b), only intended to preclude unnecessary "investigations" when the investigation is conducted by personally summoning the taxpayer. The legislative history of this section shows without dispute that its primary function is to protect the taxpayer from unnecessary annoyance and to preserve his peace of mind. It is contrary to common understanding to say that a taxpayer is not harassed or annoyed and his peace of mind not threatened when a criminal investigation is conducted of him through third parties. In fact, the peace of mind and the harassment of the taxpayer are likely to be affected and be carried to a far greater degree when the investigation does involve third parties living or working in the community of the taxpayer, and especially is this the case in our present society where criminal tax matters receive publicity to a greater degree than ever before.

The precise issue here involved, i.e., as to whether § 7605(b), I.R.C. 1954, is or is not applicable when the taxpayer is being investigated by and through third parties having knowledge and in possession of records directly bearing upon his alleged criminal liability, has been squarely before a United States District Court, but before

a United States Court of Appeals on only two occasions. The most recent consideration was, of course, the decision of the Court below. The initial decision in this area was in the Ninth Circuit in *Martin* v. *Chandis Securities Co.*, 128 F. 2d 731 (9th Cir., 1942). The Court in the latter case consisely stated the question:

> "The question is whether in investigating the return of one taxpayer, the Bureau may investigate the books of a third person regardless of whether the investigation is necessary or not. In other words, is § 3631 [now § 7605(b) I.R.C. 1954] a limitation on the power of the Bureau, or is it merely a personal right available only to the taxpayer?
>
> We believe it is the former and the Bureau has no power to make an unnecessary examination or investigation." (128 F. 2d at 735) (Brackets supplied)

In *Arend* v. *DeMasters*, 181 F. Supp. 761 (Ore. 1960), § 7605(b), I.R.C. 1954 was similarly held applicable in a proceeding by the taxpayer to enjoin a summons directed to a third party (there a bank). Accord, *Falsone* v. *United States*, 205 F. 2d 734, 742-743 (5th Cir. 1953); Cf. *O'Connor* v. *O'Connell*, 253 F. 2d 365, 370 (1st Cir. 1958). The decision below, standing alone, presents a square conflict with other decisions regarding the interpretation and scope of an important statutory enactment, and it is respectfully submitted that this Court should grant a review thereof.

In reaching its decision to limit the scope of § 7605(b) I.R.C. 1954 to direct inquiries of the taxpayer, it is respectfully submitted that the Court below failed to take cognizance of both the plurality of restrictions and the use of the word "investigations" therein contained, thereby nullifying such portions thereof, the effect of which was the modification or repeal by the judiciary of a statute enacted by Congress. In forbidding both an unnecessary "examination"[2] and "investigations," Congress must not

be presumed to have used either of the words needlessly, but rather meaning must be given to both. *United States v. Menasche*, 348 U. S. 528, 539 (1954); *F.C.C. v. Cohn*, 154 F. Supp. 899, 910 (S.D.N.Y. 1957). In fact, the use of the word "investigations" and the word "examination" in the same section must lead to the conclusion that the two words are to be given different meanings. *See, Seatrain Lines v. United States*, 168 F. Supp. 819, 825 (S.D.N.Y. 1958). It is patently obvious that the word "examination" is not so extensive as the word "investigations" and that the two must be accorded separate meanings. *Mora v. The Great Western Insurance Co.*, 23 N. Y. Super. 622, 627-628, 10, Bosworth 622, 627-628 (1863). It was the duty of the Court below to give force and effect, if possible, to every clause and word of the relevant statute. *United States v. Menasche*, 348 U. S. 528 (1954); *F.C.C. v. Cohn*, 154 F. Supp. 899, 910 (S.D.N.Y. 1957); "Courts should not use erasers on legislation but should try to give a meaning to all the terms of a statute." *Queensboro Farming Products v. Wickard*, 137 F. 2d 969, 976 (2nd Cir. 1943); *Lafrate v. The Liberte*, 106 F. Supp. 619, 621 (S.D.N.Y. 1953).

While the word "examination" may be construed to mean merely a direct personal scrutiny of the taxpayer himself, the same meaning cannot be given, under the principles of constructions set forth in the cases cited *supra*, to the word "investigations," which must be construed as an inquiry, in the broader sense, into all of the facts relating to the taxpayer as they may be gleaned from third parties. It is clear that the word "investigations" must be construed to refer to an inquiry which obtains information from third party witnesses and not merely from the party who is the subject of the investigations. *Mora v. The Great Western Insurance Co., supra; In re Securities & Exchange Commission*, 84 F. 2d 316 (2d Cir. 1936), rev'd other grounds 299 U. S. 504; *People v. One 1957 Ford Truck, etc.*, 325 P. 2d 676 (D. C. App. 2d Dist. Cal. 1958);

People v. One 1941 Chevrolet, etc., 248 P. 2d 786 (D. C. App. 2d Dist. Cal. 1952); *People v. Grossman*, 262 N. Y. Supp. 66 (Bronx, 1932); *People v. Culkin*, 248 N. Y. 465, 469 (1928); *People ex rel. Fennell v. Wilmot*, 217 N. Y. Supp. 477 (Saratoga, 1926). In *Application of Gilchrist*, 224 N. Y. Supp. 210 (N. Y., 1927), the Court stated in a reference to the word "investigation":

> "And the term has a well-defined meaning, denoting an inquiry by hearing witnesses, taking testimony and receiving full disclosure." (224 N. Y. Supp. at 220)

Most certainly an "investigation" in the case at bar would be an inquiry extending to third parties and would not be one limited to a personal examination of the taxpayer.

As recently as 1956, a United States District Court stated:

> "The Courts have not as yet had much opportunity to give specific meaning to the general language of 26 U.S.C. § 7605(b)." *In re House*, 144 F. Supp. 95, 98 (N. D. Cal. 1956).

Since that time, with the exception of the Court below, there has been little expression of judicial interpretation of this section. With the ever increasing importance of taxation and the publicity attendant thereto, this section is likely to become of increased significance to the taxpaying citizenry; and this case, therefore, presents a notable opportunity for an ultimate clarification of the meaning of 26 U.S.C. § 7605(b).

POINT II

The summary denial of petitioners' application, without a hearing, despite the existence of issues of fact, was error, a violation of their constitutional rights, and conflicts with decisions in other Circuits.

The decision below should be reviewed because it erroneously affirmed the summary denial of petitioners' application to quash certain Internal Revenue Service summonses on the grounds that the service of said summonses constituted part of a prohibited investigation within the purview of 26 U.S.C. § 7605(b).

It is clear that the question of whether action by the Internal Revenue Service does in fact constitute an investigation which is prohibited by statute presents a question of fact which must be determined upon the circumstances of the particular case. Though the District Court is undoubtedly faced thereby with a mixed question of fact and law, the Federal District Courts have had no difficulty in requiring a hearing, wherein testimony subject to the test of cross-examination is produced. *United States* v. *Lipshitz*, 132 F. Supp. 519 (E.D.N.Y. 1955); *United States* v. *American Stevedores*, 16 F.R.D. 164 (S.D.N.Y. 1954).

The government's conclusory allegation that at no time was the investigation of the taxpayers completed and that this present investigation is not a prohibited third and unnecessary investigation, is at war with petitioners' allegations. There is presented thereby a clear justiciable issue of fact which can properly and equitably be decided only through a hearing wherein the conflicting testimony is adduced and is subject to cross-examination. The precise issue in this case, i.e., whether the examination or investigation had or had not terminated so that the service of the administrative summons constituted a prohibited re-examination or investigation within the pro-

hibitions of 26 U.S.C. § 7605(b) has been before a District Court in the Ninth Circuit. Although the District Court, on the evidence and testimony presented, found for the government on this factual issue, it did so only after a full scale hearing, whereon it made findings of fact on this precise issue. *Boren* v. *Tucker*, 239 F. 2d 767 (9th Cir. 1956). In contrast, to permit the rule applied below would empower the Internal Revenue Service to avoid the restrictions of the statute and to frustrate Congressional intent by a mere conclusory allegation that the third investigation complained of is a mere continuation of the first.

The Court below summarily and purely on the basis of affidavits submitted, denied petitioners' application to quash and in like manner denied an alternative application to hold a hearing on the issues of fact raised by an application asserting the applicability of 26 U.S.C. § 7605(b).

The application below to quash Internal Revenue summonses is essentially one which is injunctive in nature. *Arend* v. *DeMasters*, 181 F. Supp. 761 (Ore. 1960); *United States* v. *United Distillers Products Corp.*, 64 F. Supp. 978 (Conn. 1946), aff'd. 156 F. 2d 872 (2nd Cir. 1946). Rule 65 of the Federal Rules of Civil Procedure requires that an application for injunctive relief shall be determined at a hearing, which means "• • • a trial of an issue of fact. Trial of an issue of fact necessitates an opportunity to present evidence." *Hawkins* v. *Board of Control*, 253 F. 2d 752 (5th Cir. 1958).

This elementary rule that a hearing, wherein the right to present and cross-examine witnesses is granted, is most certainly applicable to proceedings to quash, vacate or enjoin the enforcement of an administrative Internal Revenue Service summons; and when there is an issue of fact, this right should have been afforded to petitioners.

The cases are numerous wherein hearings to taxpayers who were contesting the legality of an Internal Revenue

Service summons were required and held. *McWhinney* v. *Cain*, 289 F. 2d 315 (3rd Cir. 1961); *O'Connor* v. *O'Connell*, 253 F. 2d 365 (1st Cir. 1958); *Beatty* v. *United States*, 227 F. 2d 350 (8th Cir. 1955); *Local 474, etc.* v. *United States*, 240 F. 2d 387 (9th Cir. 1956), (wherein the Circuit Court remanded on the grounds that the lack of a full hearing in the District Court was not conducive of a proper determination of taxpayers' rights to contest the summons); *Peoples Deposit Bank & Trust Co.* v. *United States*, 212 F. 2d 86 (6th Cir. 1954); *Falsone* v. *United States*, 205 F. 2d 734 (5th Cir. 1953); *Boren* v. *Tucker*, 239 F. 2d 767 (9th Cir. 1956); *Arend* v. *De-Masters*, 181 F. Supp. 761 (Ore. 1960); *U. S. Aluminum Siding Corp.* v. *Eshleman*, 170 F. Supp. 12 (N. D. Ill. 1958); *In re House*, 144 F. Supp. 95 (N. D. Cal. 1956); *In re Wood*, 130 F. Supp. 121 (W. D. Ky. 1955); *United States* v. *United Distillers Products Corp.*, 64 F. Supp. 978 (Conn. 1946), aff'd. 156 F. 2d 872 (2nd Cir. 1946). Even the Second Circuit early approved a procedure whereby on a motion contesting the validity of an Internal Revenue summons the matter was set down for a full factual hearing on the legality of the summons. *In re National Public Utility Investing Corp.*, 79 F. 2d 302 (2nd Cir. 1935). There the District Court went so far as to refer the issues of fact to a special master to submit factual findings thereon. Cf., *Rasquin* v. *Muccini*, 72 F. 2d 688 (2nd Cir. 1934).

In spite of the weight of authority on this point, the Court of Appeals in its opinion below, refused to consider the petitioners' alternative request that the proceeding be remanded for a full hearing on the issues of fact necessarily raised by an application under 26 U.S.C. § 7605(b). It is interesting to note that the Court of Appeals for the Ninth Circuit, in a case involving the propriety of the issuance of an administrative Internal Revenue summons, made a specific holding to the effect that the hearing held in the District Court was inadequate and accordingly

remanded the case for a full hearing on the factual issues raised by the taxpayer. *Hubner* v. *Tucker*, 245 F. 2d 35 (9th Cir. 1957). The Court of Appeals for the Ninth Circuit felt that a taxpayer's constitutional rights were not protected, and accordingly remanded the case, where there had in fact been a hearing, although not one such as to meet the requirements of due process. Compare this with the result in the court below wherein taxpayers were totally and summarily deprived of the right to present *any* testimony or test the credibility of the affiant on behalf of the government, whose affidavit constitutes the entire basis of the government's position.

In the case at bar, it is clear that the knowledge required to make a determination as to whether this investigation was in fact a prohibited third and hence unnecessary investigation or whether it was in fact merely a continuation of the same investigation, rested largely in the domain of the government. Where knowledge is thus vested in the control of one party, the right of cross-examination should not be lightly foreclosed and the matter should be decided upon testimony and not upon conclusory allegations in affidavits. *Bishop* v. *Shaughnessy*, 119 F. Supp. 62 (N.D.N.Y. 1950); *In re Brooklyn Pawnbrokers, Inc.*, 39 F. Supp. 304 (E.D.N.Y. 1941). The holding of the Court below in denying a hearing is not only in conflict with the decisions in the courts deciding the above cited cases, but it stands virtually alone in this regard, and is therefore clearly in error.

The Committee reports in reference to the predecessor of 26 U.S.C. § 7605(b) clearly indicate that the purpose of this remedial statute is to protect taxpayers from harassing unnecessary examination and investigations. S. R. No. 275, 67th Cong. 1st Sess., Sept. 26, 1921, Cum. Bull. 1939-1, pt. 2, pp. 181, 203; 61 Cong. Rec. 5855; *O'Connor* v. *O'Connell*, 253 F. 2d 365, 370 (1st Cir. 1958). The Court in the *O'Connor* case wisely rejected the

government's view that mere conclusory allegations were sufficient to overcome the bar of § 7605(b) and stated that to hold otherwise would relegate the Court to the position of summarily affixing its stamp of approval to administrative action. The Court stated further that Congress clearly intended to give taxpayers this much protection, and that such procedure would not unduly hamper the program of the Internal Revenue Service.

This Court has recently set forth its position with regard to the action of courts in reaching decisions concerning the validity of administrative action solely upon affidavits and without resort to the benefit of actual testimony received through the lips of witnesses subject to cross examination; and such position has evinced an attitude of condemnation in reference to such a summary procedure. *Greene* v. *McElroy*, 360 U. S. 474, 3 L. ed. 2d 1377, 1390, 1397 (1959). There the Court (through Mr Chief Justice Warren) stated:

> "Certain principles have remained relatively immutable in our jurisprudence. One of these is that where governmental action seriously injures an individual, and the reasonableness of the action depends on fact findings, the evidence used to prove the Government's case must be disclosed to the individual so that he has an opportunity to show that it is untrue. While this is important in the case of documentary evidence, it is even more important where the evidence consists of the testimony of individuals whose memory might be faulty or who, in fact, might be perjurers or persons motivated by malice, vindictiveness intolerance, prejudice, or jealousy. We have formalized these protections in the requirements of confrontation and cross examination. They have ancient roots. They find expression in the Sixth Amendment which provides that in all criminal cases the accused shall enjoy the right 'to be confronted with the witnesses against him.' This Court has been zealous to protect these rights

> from erosion. It has spoken out not only in criminal cases (Citations omitted), but also in all types of cases where administrative and regulatory actions were under scrutiny." 360 U. S., at 496.

This Court went on to hold that before a person can be summarily deprived of a right without a full hearing, it must be clear that Congress has explicitly authorized a procedure which denies the safeguards of confrontation and cross-examination.

In the present case, not only is it evident that Congress has not specifically sanctioned the imposition of such summary powers as were condemned by this Court in *Greene* v. *McElroy, supra*, but conversely it is clear that Congress expressly indicated an intention to require a hearing in proceedings to contest the legality of an Internal Revenue Service summons on the grounds that said summons constitutes a violation of 26 U.S.C. § 7605(b). 26 U.S.C. § 7602, *et seq.*, relating to the issuance and enforcement of an Internal Revenue Service summons makes reference to a hearing to be held in connection with an enforcement of the summons. Since § 7602, *et seq.*, is to be read in conjunction with § 7605(b), it is apparent that there is a clearly expressed Congressional intent to require a hearing in applications made under 26 U.S.C. § 7605(b). *U. S. Aluminum Siding Corp.* v. *Eshleman*, 170 F. Supp. 12 (N. D. Ill. 1958). The decision of the Court below was in direct contravention of a stated Congressional policy and was, therefore, error.

A Special Agent of the Internal Revenue Service, such as we have in the case at bar, as distinguished from a Revenue Agent, is responsible for the conduct of investigations instituted *for the sole purpose of gathering evidence to support a criminal prosecution. Russo* v. *United States*, 241 F. 2d 285 (2nd Cir. 1957); *United States* v. *Wolrich*, 129 F. Supp. 528 (S.D.N.Y. 1955); *United States* v. *Lipshitz*, 132 F. Supp. 519 (E.D.N.Y. 1955). In this criminal tax area in particular, the courts should be particularly

sensitive to the insidious extension of massive government control infringing upon individual rights. Cf. *Zimmerman* v. *Wilson*, 81 F. 2d 847, 849 (3d Cir. 1936).

> "The field of taxation represents probably the greatest single area of contact between individuals and the force of the state." *In re House*, 144 F. Supp. 95 (N. D. Cal. 1956).

It is interesting to note that in proceedings analogous to the one now before this Court, namely, one to enjoin the collection of taxes, the District Court held a full scale hearing equivalent in scope to that of the usual trial. *Enoch* v. *Williams Packing*, 291 F. 2d 402 (5th Cir. 1961). Significantly, this Court has granted certiorari in this case. *Enoch* v. *Williams Packing*, 7 L. ed. 2d 336 (1961). The problem was whether on the facts there present the Court should enjoin the collection of taxes in contravention of a statute prohibiting injunctions with regard to the collection of taxes. If this Court is disposed to grant certiorari in a case wherein the question is whether there should be an equitable exception to a tax provision [26 U.S.C. § 7421(a)], surely it should grant review in a case where an express Congressional direction has been directly repudiated by the Court below.

CONCLUSION

For the reasons stated, the petitioners respectfully pray that the Writ of Certiorari be granted.

Respectfully submitted,

Boris Kostelanetz,
Attorney for Petitioners.

Corcoran, Kostelanetz, Gladstone & Lowell, Esqs.,
Jules Ritholz, Esq.,
Jon H. Hammer, Esq.,
Of Counsel.

APPENDIX

Opinion of United States Court of Appeals.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 231—September Term, 1961.

(Argued January 19, 1962 Decided February 13, 1962.)

Docket No. 27174

Application of

PERCY C. and MARGARET A. MAGNUS

to quash certain summonses issued by the Internal Revenue Service to testify, and produce records, etc.,

Petitioners-Appellants,

UNITED STATES OF AMERICA,

Respondent-Appellee.

Before:

MEDINA, MOORE and SMITH,

Circuit Judges.

Appeal by taxpayers from an order of the United States District Court for the Southern District of New York, Edward J. Dimock, *Judge*, denying a motion to quash two summonses directed to third parties on the ground that taxpayers had no standing to object under Section 7605(b) of the Internal Revenue Code of 1954. Opinion below reported at 196 F. Supp. 127.

Affirmed.

Appendix

BORIS KOSTELANETZ, New York, N. Y. (Corcoran, Kostelanetz, Gladstone & Lowell, New York, N. Y., on the brief; Jules Ritholz, of counsel), *for the petitioners-appellants.*

JOHN E. X. PELOSO, Assistant United States Attorney, Southern District of New York (Robert M. Morgenthau, United States Attorney for the Southern District of New York, on the brief; Morton L. Ginsberg, Assistant United States Attorney, of counsel), *for the respondent-appellee.*

MOORE, *Circuit Judge*:

Percy C. and Margaret A. Magnus (referred to as "the taxpayers") whose income tax liability for the years 1948 through 1957 is under investigation by agents of the Internal Revenue Service (IRS) appeal from an order denying a motion to quash two summonses issued under authority of Section 7602, Internal Revenue Code of 1954 (the Code). One summons was directed to a corporation, Magnus, Mabee & Reynard, Inc., of which Percy C. Magnus is president, a director and a stockholder; the other was directed to the firm, Hurdman & Cranstown, Certified Public Accountants, which performed services for the corporation (including the preparation of tax returns) and for Mr. Magnus personally.

Section 7602, "Examination of books and witnesses," gives to the Secretary or his delegate broad powers "to examine any books, papers, records, or other data which may be relevant or material to such inquiry [i.e., ascertaining correctness of any return, determining or collecting any liability]." He may also summon any person deemed proper to produce books and records containing entries

relating to the business of the taxpayer under investigation and to take relevant or material testimony. Accordingly, the Secretary served summonses not upon the taxpayers but upon third parties to give testimony and produce certain specified records. These third parties did not appear upon the motion to quash and object that their appearance to give testimony or the production of records would be "unreasonably onerous" or that the information sought is not "material and relevant to the investigation" (*Foster* v. *United States*, 2 Cir., 1959, 265 F. 2d 183, 186, cert. denied 360 U. S. 912 (1959)).

That these "considerations constitute the criteria for judicial enforcement of subpoenas issued by various administrative agencies is well established: an affirmative showing of probable cause for the administrative inquiry is not required. [Citing cases.]" *Ibid.* We have held that: "The same principles and the same criteria are applicable to the enforcement of Internal Revenue subpoenas. [Citing cases.]" *Ibid.* In *Foster* a summons was served on the New York Agency of a foreign bank to produce records of the taxpayers under investigation. Failure to obey brought about the issuance of an *ex parte* order directing compliance which the Bank sought to have vacated. At this point, the taxpayers moved to intervene, which motion unopposed was granted. The taxpayers were the appellants, the Bank apparently being willing to abide the event and not claiming that the summons was overburdensome or called for records which were irrelevant and immaterial. The taxpayers, in objecting to the summons, asserted that on the merits any tax claim against them was barred by the statute of limitations; hence, they argued that the examination was "unnecessary and unreasonable." This court affirmed the denial of the motion to vacate.

Appellants in the case now before us, as they did in the court below, endeavor to bring themselves within the pro-

visions of Section 7605(b)[1] of the Code which deals with "Restrictions on examination of taxpayer." This section has no bearing on the issue now before us. The examination which IRS seeks is of third parties and not a further examination of the taxpayer. The inspection desired is of corporate books and accounting firm papers and not of the taxpayer's books. Under these circumstances, the taxpayers have no standing to quash the summonses which call neither for their further appearance or examination nor for further production of their books.

Although headings are not to be read as a limitation on the multiple purposes of a statute (*Railroad Trainmen v. Baltimore & O. R. Co.*, 331 U. S. 519, 528 (1947)), Section 7605(b) itself clearly reveals the accuracy of the heading. It deals with taxpayers and restrictions for their own protection, specifically reading, "No taxpayer shall be subjected to unnecessary examination or investigations, * * *." These words cannot be so construed as to bestow upon the taxpayer the privilege of forcing IRS to show cause why its investigations of records and other information in the hands of third parties are necessary every time that some source is discovered which might throw some light on the tax audit. An intolerable situation would be created, which would seriously impair any effective investigation, were the taxpayer allowed, by injunction or motion to vacate, to compel IRS to disclose information already obtained and what it hoped to secure through its various summonses. Such a procedure would be tantamount to the supplying to the taxpayer of a continuous bill of particulars as to each stage of the government's case.

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[1] § 7605(b): Restrictions on examination of taxpayer: No taxpayer shall be subjected to unnecessary examination or investigations, and only one inspection of a taxpayer's books of account shall be made for each taxable year unless the taxpayer requests otherwise or unless the Secretary or his delegate, after investigation, notifies the taxpayer in writing that an additional inspection is necessary.

A construction limiting the section to its unambiguous language is not unfair to the taxpayer. It protects him from unnecessary examinations or investigations. An investigation, however, often requires a long period of time. There may be many ramifications which lead into many areas. Each new clue investigated is not a new investigation in a Section 7605(b) sense. A taxpayer cannot properly claim that because IRS has summoned six third parties it cannot summon six additional without showing good cause. The investigation continues until completed as one investigation.

As to third parties, they have the protection always accorded to them by the courts which limit burdensome subpoenas, restrict them to relevant material and refuse to permit unwarranted searches and seizures. As to taxpayers, nothing said so far prevents them from enjoying the benefits of the section. Where a taxpayer is subjected to unnecessary examinations and investigations, he may seek court recourse. If more than one inspection of his books is sought for any one year, he may insist on the statutory notice. However, "Our courts should not permit interventions which delay government action at the investigation stage unless the interest asserted is direct and immediate" (Lumbard, *Ch.J.*, in *Foster, supra*, p. 189).

We have reviewed the many cases cited by both parties. Because of the special circumstances of each case, they are not particularly helpful. Where the statute is clear, it is frequently unwise to try to construe it in accordance with language used in opinions in other cases, which applies most pertinently only to the facts of those cases. However, in a more general vein, "The suppression of truth is a grievous necessity at best, more especially when as here the inquiry concerns the public interest; it can be justified at all only when the opposed private interest is supreme" (*McMann v. Securities and Exchange Commission*, 2 Cir.,

1937, 87 F. 2d 377). But here there is no "opposed private interest." No claim is made that the testimony or documents sought would be privileged or that they would not be material or relevant to the investigation.

In view of our belief that the taxpayers cannot rely on Section 7605(b) in the instant case, it is unnecessary to discuss the questions of burden of proof of necessity or probable cause. In passing, however, it may be said that were the government forced to establish the necessity for every phase of its investigations into taxpayers' financial affairs before proceeding, "it is impossible to see how the statutes can be enforced at all, or how any wrongdoer can be brought to book" (*McMann, supra*, p. 379).

Order affirmed and stay vacated.

Appendix

Order.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

* * * * *

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the thirteenth day of February one thousand nine hundred and sixty-two.

Present: HON. HAROLD R. MEDINA,
HON. LEONARD P. MOORE,
HON. J. JOSEPH SMITH,
Circuit Judges.

IN THE MATTER

of

the Application of PERCY C. and MARGARET A. MAGNUS,

Petitioners-Appellants.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record fom the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order of said District Court be and it hereby is affirmed.

It is further ordered that the stay heretofore granted by said District Court be and it hereby is vacated.

A. DANIEL FUSARO,
Clerk.

Appendix

Petition for Rehearing.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

SEPTEMBER TERM, 1961—No. 231

DOCKET NO. 27174

APPLICATION OF

PERCY C. and MARGARET A. MAGNUS to quash certain summonses issued by the INTERNAL REVENUE SERVICE to testify and produce records, etc.

The appellants above named respectfully petition this Honorable Court for a rehearing, pursuant to Rule 25 of the Court of Appeals for the Second Circuit, of the appeal in the above entitled cause argued before the Honorable Harold R. Medina, presiding, Honorable Leonard P. Moore and Honorable J. Joseph Smith, Circuit Judges, on January 19, 1962, and decided on February 13, 1962, opinion by Moore, Circuit Judge.

This appeal is before this Court on a claim by appellants that an Internal Revenue Service reinvestigation to which they are being subjected is unnecessary within the meaning of Section 7605(b) because it is the third consecutive one conducted in relation to the same tax liability for the same taxpayers for the same period of years twice before scrutinized, after each of which prior investigations the Government marked the matter closed.

In the alternative to their prayer for a rehearing, the appellants respectfully pray that the appeal be reargued *en banc* pursuant to 28 U.S.C.A., Section 46, Subdivision (c). [*Western Pacific Ry. Corp.* v. *Western Pacific Ry. Co.*, 345 U. S. 247, 97 L. Ed. 986 (1953).] It is most respectfully submitted that a hearing *en banc* is indicated because the opinion and decision of this Court adversely affects the civil rights of taxpayers and has the effect of modifying or repealing a statute of Congress.

In support of this petition, appellants represent to the Court as follows:

The argued position of the appellants as to each of the points of appeal is respectfully reserved but this petition is devoted to convincing the Court that it has overlooked the statutory language and the legislative history in construing Section 7605(b), I.R.C. 1954; that it has overlooked the undenied fact that the investigation which evoked this appeal has as its subject the appellants and not the persons summoned; and that it has overlooked appellants' contention that if they have any burden of proof they are entitled to a hearing at which they may discharge it.

POINT I

THE COURT OVERLOOKED THAT THE FOSTER CASE AND SECTION 7602 OF THE INTERNAL REVENUE CODE ARE NOT THE SOLE CRITERIA FOR JUDICIAL ENFORCEMENT OF INTERNAL REVENUE SERVICE SUMMONSES BUT THAT SECTION 7605(b) ALSO APPLIES.

In its opinion of affirmance, the Court held that the criteria stated in *Foster* v. *United States*, 265 F. 2d 183 (2nd Cir. 1959), cert. den. 360 U. S. 912, are those to be considered in a proceeding relating to administrative subpoenas. By reason of its subsequent exclusion of Section 7605(b) from consideration, it was the Court's ruling that

the criteria of the *Foster* case and, of course, the provisions of Section 7602 of the Internal Revenue Code, are the sole criteria to be considered.

The Congressional scheme for Discovery of Liability is apparent from the structure of the Internal Revenue Code. Chapter 78 of the Code, which includes all sections here relevant, relates to Discovery of Liability and Enforcement. Sub Chapter A of Chapter 78, which includes all the sections here relevant, relates to examination and inspection. While Section 7602 of Sub Chapter A provides for the administrative summons, Section 7605(b), its companion section in the same Sub Chapter restricts the examination referred to in Section 7602. It would seem indisputable that all the sections of Sub Chapter A being in *pari materia* should be construed together.

It is respectfully submitted that the Court misconstrued Section 7605(b) by holding in effect that only third parties summoned as part of an unnecessary investigation of the taxpayers may assert rights under that section. Such construction is contrary to the manifest intent of the Statute and of the intent of Congress as expressed by Senator Penrose, during the debate on the section:

> "Mr. President, the provision is entirely in the interest of the taxpayer and for his relief. . . ." (61 Cong. Rec. 5855, Appellants' Brief, p. 24)

The Court, it is most respectfully urged, misconstrued the section, in rendering into nullity the use by Congress of the plural for the word "investigations". This was the effect because of the holding by the Court that all investigations, no matter how often repeated and completed, continue until again completed as a single investigation. This is contrary to the grammatical construction of the Statute and to the legislative history which discloses Congressional dissatisfaction with repeated investigations and which led to the use of the plural which the decision disregards. To

hold that Section 7602 establishes criteria for summonses requires that the criteria of Section 7605(b) also be applied. To hold otherwise deprives the latter section of meaning. Either it circumscribes the Internal Revenue Service investigation and its summonses or it does not have meaning. This Court has held that ". . . Courts should not use erasers on legislation but should try to give a meaning to all the terms of a statute. . . ." *Queensboro Farming Products* v. *Wickard*, 137 F. 2d 969, 976 (2nd Cir. 1943).

POINT II

THE COURT OVERLOOKED THAT SECTION 7605(b) CONTAINS THREE RESTRICTIONS, TWO OF WHICH ARE APPLICABLE TO THE INSTANT CASE AND HAVE BEEN VIOLATED BY THE INTERNAL REVENUE SERVICE.

It is most respectfully submitted that in its opinion of affirmance the Court has overlooked the plurality of restrictions contained in Section 7605(b) of the Internal Revenue Code of 1954 and the Congressional intent manifest in the language therein contained. It is uncontroverted in this appeal that Section 7605(b) imposes restrictions on two areas of activity of the Internal Revenue Service, the first of which restriction is dual. This was the interpretation of the Court below and is not controverted by the Government. Indeed, it will be noted that the heading of Subdivision (b) contemplates a plurality of restrictions in its use of the plural of the word "Restrictions." The separate and distinct restrictions of Section 7605(b) are as follows:

1. (a) No taxpayer shall be subjected to an unnecessary *examination.*

   (b) No taxpayer shall be subjected to unnecessary *investigations.*

Appendix

II (a) Only one *inspection* of taxpayer's books of account per year.

(b) An additional *inspection* if, after investigation, secretary or his delegate notifies taxpayer in writing that an additional inspection is necessary.

Under the subdivisions of the first restriction, Congress has forbidden both an unnecessary "examination" and unnecessary "investigations". In forbidding both, the legislature must not be presumed to have used either of the words needlessly and meaning should be given to both of them. It is the Court's duty to give effect, if possible, to every clause and word of the Statute. *United States* v. *Menasche*, 348 U. S. 528, 539, 99 L. Ed. 615, 624 (1954); *F.C.C.* v. *Cohn*, 154 F. Supp. 899, 910 (S.D.N.Y. 1957). This view is supported by Congress' use of the singular for "examination" and the plural for "investigations". Any other construction of the section would strip the Statute of its meaning by overlooking the presence of both the word "examination" and the word "investigations."

POINT III

THE COURT OVERLOOKED THAT THE CONDUCT COMPLAINED OF IS AN INTERDICTED INVESTIGATION BY THE INTERNAL REVENUE SERVICE OF THE APPELLANTS, NOT OF THE WITNESSES SUMMONED.

In holding Section 7605(b) inapplicable, this Court stated that what the Internal Revenue Service seeks is an examination of third parties and not a further examination of the taxpayers. In so holding, the Court overlooked the undisputed fact that what the Internal Revenue Service is conducting and what the taxpayer seeks to restrict, as forbidden by the Statute, is an *investigation of*

the taxpayers. The application is not to restrict an investigation of the witnesses summoned. Indeed, the witnesses summoned are not under investigation. That this is the fact is demonstrated by the summonses themselves (App. 9a-12a) which are encaptioned in the matter of the tax liability of the appellants. It is also demonstrated by the undenied, uncontroverted affidavit of the appellant that the summonses were issued in furtherance of this investigation (App. 6a, ¶9). Indeed, it is acknowledged by the Special Agent himself who signed the summonses (App. 10a-12a) and in his own affidavit in which he characterizes the activity of the Internal Revenue Service as an investigation (App. 14a, *et seq.*).

In characterizing the activity of the Internal Revenue Service as an examination of third parties, this Court apparently construes the word "examination" to mean a direct personal scrutiny and restricts its applicability to the third parties under direct scrutiny. Under such construction, the activity petitioners complain of would concededly not fall within the meaning of the word "examination" as used in Section 7605(b). But in ending the analysis there, the Court most respectfully overlooked the word "investigations" which describes another kind of activity also forbidden. If examination be construed as direct scrutiny, the same meaning cannot, under established principles of construction, be given the word "investigations" which must then be construed as an inquiry, in the broader sense, into all the facts relating to the taxpayer as they may be gleaned from examination of the taxpayer and others. This is consistent with the distinction made in the Internal Revenue Agents Manual between a Revenue Agent's examination and a Special Agent's investigation (Appellant's brief, p. 17). To give "examination" and "investigations" the same meaning, is to presume, contrary to the Canons of Construction, that Congress used words uselessly.

"It is a basic rule of statutory construction that the legislature is presumed to have used no superfluous words and that significance should ordinarily be given to every word in a statute." *Lafrati v. C.I.R.*, 106 F. Supp. 649, 621 (S.D.N.Y. 1953), Weinfeld, J.

The Court overlooked that the proposed examination of the persons summoned is part of an investigation of appellants which, if unnecessary, is forbidden by the Statute. If forbidden by the Statute, then the aggrieved party whom the Statute protects certainly has standing to seek its protection. That is what Congress intended.

POINT IV

THE COURT OVERLOOKED THAT REGARDLESS OF WHICH PARTY HAS THE DUTY OF SHOWING CAUSE ON THE EXAMINATION OF THIRD PARTIES OR THE BURDEN OF PROOF ON THE ISSUE OF NECESSITY, THE DENIAL OF A HEARING PREVENTED THE REQUISITE SHOWING BY WHICHEVER PARTY MUST BEAR THE BURDENS.

Most respectfully we urge that the Court misconceived appellants' position with respect to the examination of third parties. Appellants do not contend that the duty to show cause is on the Internal Revenue Service in every case where third parties are summoned. The contention is that such duty exists where the summoning of third parties is part of an investigation, interdicted because unnecessary.

While it seems cogent, appellants do not rest their claim that the investigation is unnecessary on the fact that every penny of tax liability plus interest as computed by the Government has been paid. The record discloses allegations that the present investigation is unnecessary because it is the third consecutive one conducted in relation to the same tax liability for the same taxpayers for the same period of years previously scrutinized and where after

each prior investigation the Government marked the matter closed. Appellants were denied the opportunity to prove these allegations below. On appeal, they were defeated because they *failed* to prove the allegations below. Caught in such whiplash the protection of Section 7605(b) is rendered a nullity. The same quandry exists with respect to bearing the burden of proof where the denial of the hearing below deprives appellants of an opportunity to bear the burden and the affirmance on appeal is based upon a failure to bear the burden. Any ruling with respect to which party must show cause and bear the burden of proof on necessity has implicit in it a requirement that a hearing be held.

Appellants do not claim "that because the Internal Revenue Service has summoned six third parties it cannot summon six additional without showing good cause." Incontrovertibly the Internal Revenue Service may summon as many witnesses as are necessary in one necessary investigation. But if Section 7605(b) is to have any meaning at all the Internal Revenue Service may not summon even a single witness in an unnecessary investigation. The question whether this is a continuing investigation or a third unnecessary investigation has never been factually determined at any hearing or otherwise.

While the ruling in *McMann* v. *S.E.C.*, 87 F. 2d 377 (2nd Cir. 1937) is the proper one in investigations affecting the investing public in the financial community at large, even that decision recognizes the weighty balance of an opposed private interest. Here in a tax investigation of individual taxpayers the equities present in investigations directly affecting a large segment of our population are lacking. The statute affording protection to private citizens from overreaching on the part of a huge powerful administrative agency should be given force and meaning and is consistent with the American tradition of balancing the individual rights of single persons against the weighty power of anonymous, and sometimes overzealous bureaucracy.

WHEREFORE, on the foregoing reasons and for the reasons appearing in appellants' brief and reply brief it is respectfully prayed that this petition for rehearing be granted, that upon rehearing the Court reconsider its decision herein and that the judgment of the District Court be reversed, that the order below be vacated and entry directed of an order quashing the Internal Revenue summonses and staying further investigation of appellants by the Internal Revenue Service for the taxable years 1948 through 1957 or in the alternative that the proceedings be remanded to the United States District Court for a hearing on the necessity of this third investigation and that the mandate of this Court be stayed pending the disposition of this petition.

Respectfully submitted,

CORCORAN, KOSTELANETZ, GLADSTONE & LOWELL.

BORIS KOSTELANETZ, Esq.,
JULES RITHOLZ, Esq.,
EDWARD J. DAUS, Esq.,
Of Counsel.

CERTIFICATE.

The undersigned, attorneys for the petitioners herein, hereby certify that in their opinion, there is good ground for the foregoing petition, that it has been presented in good faith and not for the purpose of delay.

Dated: New York, N. Y., February 27, 1962.

CORCORAN, KOSTELANETZ, GLADSTONE & LOWELL.

By: B... KOSTELANETZ.

Appendix

Order.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Application of

PERCY C. and MARGARET A. MAGNUS to quash certain summonses issued by the INTERNAL REVENUE SERVICE to testify and produce records, etc.

Before MEDINA, MOORE and SMITH, Circuit Judges.

On Petition for Rehearing

Corcoran, Kostelanetz, Gladstone & Lowell, New York, N. Y. (Boris Kostelanetz, Jules Ritholz and Edward J. Daus, Of Counsel), for appellants.

Petition denied.

L. P. M.

J. J. S.

per Jane Burke
U. S. C. JJ.

March 8, 1962

Appendix

Petition for Rehearing *in Banc.*

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Application of PERCY C. and MARGARET A. MAGNUS to quash certain summonses issued by the Internal Revenue Service to testify, and produce records, etc.,

Petitioners-Appellants,

UNITED STATES OF AMERICA,

Respondent-Appellee.

Corcoran, Kostelanetz, Gladstone & Lowell, New York, N. Y., for petitioners-appellants.

No active circuit Judge having requested that the case be reheard in banc, the petition is denied.

J. EDWARD LUMBARD,
Chief Judge.

20 Mar. 1962

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641587—62

In the Supreme Court of the United States

OCTOBER TERM, 1961

No. 916

PERCY C. AND MARGARET A. MAGNUS, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinions of the district court (R. 18a–19a, 21a) [1] are reported at 196 F. Supp. 127. The opinion of the court of appeals (Pet. 20–25) is reported at 299 F. 2d 335.

JURISDICTION

The order of the court of appeals was entered on February 13, 1962. (Pet. 26.) A petition for rehearing was denied on March 8, 1962. (Pet. 36.) A petition for rehearing *en banc* was denied on March 20, 1962. (Pet. 37.) The petition for a writ of certio-

[1] References designated "R." are to the appendix to petitioners' brief in the court of appeals.

rari was filed on April 28, 1962. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether the district court properly denied taxpayers' motion to quash Internal Revenue summonses, issued during an investigation of their income tax liabilities, which called for the testimony and records of third parties not previously sought.

STATUTES INVOLVED

Internal Revenue Code of 1954:

SECTION 7602. EXAMINATION OF BOOKS AND WITNESSES.

For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary or his delegate is authorized—

(1) To examine any books, papers, records, or other data which may be relevant or material to such inquiry;

(2) To summon the person liable for tax or required to perform the act, or any officer or employee of such person, or any person having possession, custody, or care of books of account containing entries relating to the business of the person liable for tax or required to perform the act, or any other person the Secretary or his delegate may deem proper, to appear before

the Secretary or his delegate at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under oath, as may be relevant or material to such inquiry; and

(3) To take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry.

(26 U.S.C. 1958 ed., Section 7602.)

SECTION 7605. TIME AND PLACE OF EXAMINATION.

* * * * *

(b) *Restrictions on Examination of Taxpayer*—No taxpayer shall be subjected to unnecessary examination or investigations, and only one inspection of a taxpayer's books of account shall be made for each taxable year unless the taxpayer requests otherwise or unless the Secretary or his delegate, after investigation, notifies the taxpayer in writing that an additional inspection is necessary.

(26 U.S.C. 1958 ed., Section 7605.)

STATEMENT

In June 1958 the Internal Revenue Service began an investigation of the tax liabilities of petitioners, Percy C. and Margaret A. Magnus. Internal Revenue Agent Victor Blatt was initially assigned to the matter and remained assigned at the time of the proceedings here involved. At separate times the following other Special Agents were assigned to work jointly with him: Victor Biskup, John J. McLoughlin, Joseph H. Gillespie and George Alderman. (R. 14a.)

As of the time of the proceedings below, the investigation had revealed that, prior to the examination instituted by Agent Blatt, petitioners had never filed income tax returns or paid taxes they owed for the years 1948 through 1957. They had failed to file returns "reflecting approximately $1,000,000 of personal income" during those years. (R. 15a.)

On June 19, 1961, two Internal Revenue Service summonses were issued by Special Agent Alderman. One of these summonses, addressed to Magnus, Mabee & Reynard, Inc. (a corporation of which petitioner Percy C. Magnus was the president, a director and a stockholder), called for testimony by corporate officials relating to the liability of petitioners for the period 1948–1957, inclusive, and for the production of certain designated corporate books and records. The second summons, calling for testimony and the production of records relating to petitioners' liabilities for the same period, was addressed to Hurdman & Cranstoun (certified public accountants whose services were used by petitioner Percy C. Magnus and by the corporation). (R. 4a, 9a–10a, 11a–12a.)

On June 28, 1961, Percy C. Magnus petitioned the district court for an order quashing the summonses. The petition, which was in the form of an affidavit, alleged that in 1959 petitioner was the subject of an investigation conducted by Special Agent Biskup (par. 3); that the latter had "found at least preliminarily that the evidence did not support a possible charge of willfulness" (a finding "presumed" to be "embodied in a written report") (par. 5); that in the summer of 1960 Special Agent Gillespie conducted "a new investiga-

tion relating to the same years and having the same subject matter" (par. 6); that "The investigation was once again terminated", Gillespie having "made a finding [presumably "embodied * * * in a written report"] that there was an absence of willfulness", with consequent referral of the matter "back to the Audit Division of the Service" (par. 7); and that "The matter again appeared to be finally closed until May 24, 1961 when I was advised through my lawyer that a third Special Agent, George Alderman," came into the matter (par. 8). (R. 4a–6a.)

In response to the petition, the government submitted an affidavit of Special Agent Alderman which stated (R. 14a–15a):

* * * * *

> 3. At no time since June, 1958, has the investigation into the affairs of the above-named taxpayers been concluded. At no time has any formal notice been sent to the taxpayers of the termination of this investigation.
>
> 4. The procedures of the Internal Revenue Service in all income tax examinations of this nature require that at the conclusion of said examination, a report be furnished to the taxpayer wherein he is advised that the examination has resulted in a deficiency and additional taxes are due. At the same time, the taxpayer is sent a Waiver of Restrictions on Assessment and Collection of Deficiency in Tax and Acceptance of Overassessment (Internal Revenue Form 870). If the taxpayer accepts the proposed tax changes, he signs and returns the waiver, Form 870. No such revenue agent's

report or waiver, Form 870, has been sent Percy C. and Margaret A. Magnus.

* * * * *

The district court denied the motion to quash the summonses. The court ruled that petitioners had not attempted "to show that the investigation that is going on is unnecessary" (R. 19a) and that no hearing was required since "no issue [in that respect] is tendered". (R. 21a.)[2] The court of appeals affirmed. It held that the prohibition in Section 7605(b) of subjecting taxpayers to "unnecessary examination or investigations" was inapplicable to an examination of third parties and that petitioners had no standing to quash summonses which called neither for their appearance or examination nor for production of their books. (R. 23, 26.)

ARGUMENT

Section 7602 of the Internal Revenue Code of 1954 (*supra*, p. 2) gives the Internal Revenue Service broad authority to examine books and records, and to compel testimony, relating to tax liability. Section 7605(b) provides, however, that no taxpayer "shall be subjected to unnecessary examination and investigations." Petitioners contend that since several agents

[2] Presumably addressing itself to petitioners' erroneous conception that Section 7605(b) of the 1954 Code entitled them to notification in writing that an additional inspection was necessary, the district court correctly pointed out (1) that the statute required notice to be given only where more than one inspection of a *taxpayer's books of account* are made for each taxable year and (2) that the summonses here involved sought an examination of third party, not petitioners', books and records (R. 18a–19a).

had examined them and their books and records over a three-year period, the subsequent attempt by the government to examine the books and records, and to take the testimony of, third persons not previously examined, constituted an "unnecessary" examination or investigation prohibited by Section 7605(b). Both courts below correctly rejected this contention and refused to quash the administrative summonses directed to the third persons. The proposed examination of such persons and their books and records was not "unnecessary" but, on the contrary, was an appropriate step in continuing the existing investigation of petitioners' apparent failure to file income tax returns covering substantial tax deficiencies over a ten-year period. There is no conflict of decisions, and further review is unwarranted.

1. The summonses in question, issued on June 19, 1961, sought for the first time the testimony and records of third parties in connection with an investigation of petitioners' tax liabilities which had begun in June, 1958. Petitioners do not dispute Special Agent Alderman's assertion under oath that they failed, prior to the inception of the investigation, to file returns for the period 1948 to 1957 which should have reported "approximately $1,000,000 of personal income". (R. 15a.) Nor do petitioners contend that the testimony and records sought were not germane to the investigation of petitioners' tax liabilities. Their contention is that the investigation of those liabilities, although initially authorized by Section 7602 of the Internal Revenue Code of 1954, *supra*, was in fact concluded by the time the summonses in ques-

tion were issued, and that therefore any subsequent examination of the hitherto uninspected third party records and any questioning of the hitherto uninterrogated officials of the corporation and accounting firm were "unnecessary."

The basic fallacy in petitioners' contention, as the district court observed (R. 19a, 21a), is that there is no necessary connection between an allegation that the investigation had concluded and a conclusion that a subsequent investigation is "unnecessary". Even if it were assumed that the investigation of petitioners' tax liabilities had been concluded at the time the summonses to the third parties were issued, it would not follow that a re-investigation based on hitherto unexamined witnesses and records would be "unnecessary" in the Section 7605(b) sense. On the contrary, such new material may make a further investigation particularly necessary.

Moreover, petitioners' moving papers were inadequate to raise any issue as to whether the investigation of petitioners' tax liabilities had in fact been terminated. The affidavit of petitioner Percy C. Magnus (R. 4a–8a) does set forth the fact of successive participation in the investigation by three different agents, and alleges that these examinations—made without the records or testimony sought by the instant summonses—failed to establish the element of willfulness in petitioners' violations of the tax laws during the years under investigation. But a single

investigation is comprised of many steps and may involve the participation of several agents. As the court of appeals aptly pointed out (Pet. 24): "An investigation * * * often requires a long period of time. There may be many ramifications which lead into many areas. Each new clue investigated is not a new investigation in a Section 7605(b) sense." To hold otherwise would be to create an "intolerable situation * * * which would seriously impair any effective investigation"—a situation in which a taxpayer would be "allowed, by injunction or motion to vacate, to compel IRS to disclose information already obtained and what it hoped to secure through its various summonses". (Pet. 23.)

Finally, on the record in this case petitioners had no standing to quash the summonses. The court below correctly held that the restrictions of Section 7605(b) should not be construed to permit taxpayers, whose personal testimony and records are not sought, to question the otherwise ostensibly proper interrogation of third parties and the inspection of third party records, especially where, as here, such interrogation and inspection had not previously been undertaken. As the court of appeals noted (Pet. 24), third parties "have the protection always accorded to them by the courts which limit burdensome subpoenas, restrict them to relevant material and refuse to permit unwarranted 'searches and seizures" and "interventions which delay government action at the investigative

stage" should not be permitted "unless the interest asserted is direct and immediate". *Foster* v. *United States*, 265 F. 2d 183, 189 (C.A. 2d), certiorari denied, 360 US 912. Petitioners did not show any such "direct and immediate" interest.

2. There is no conflict in decisions. *Martin* v. *Chandis Securities Co.*, 128 F. 2d 731 (C.A. 9th) is distinguishable. There, the government instituted an enforcement proceeding to obtain third party records and it was held that the third party could invoke the predecessor provisions of Section 7605(b) to prevent the government from obtaining an order requiring the production of records which were shown, to the court's satisfaction, to be unnecessary to any investigation. Here the taxpayer-petitioners and not the affected third parties moved to quash summonses seeking third party testimony and records, and the record does not contain allegations of facts showing that the investigation is unnecessary.[3]

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[3] Even on its own limited ground *Martin* v. *Chandis Securities* is out of harmony with this Court's more recent pronouncements of the minimal showing required to enforce administrative subpoenas. See *Civil Aeronautics Board* v. *Hermann*, 353 U.S. 322; *United States* v. *Morton Salt Co.*, 338 U.S. 632; *Oklahoma Press Pub. Co.* v. *Walling*, 327 U.S. 186, 208. See also *Foster* v. *United States*, 265 F. 2d 183, 186 (C.A. 2d) and Judge Pope's dissent in *Local 174, Etc.* v. *United States*, 240 F. 2d 387, 393, 395 (C.A. 9th).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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No. 916

IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

PERCY C. and MARGARET A. MAGNUS,
Petitioners

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR PETITIONERS

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Argument

1. The government, at page 5 of its responding brief, relies upon the affidavit of Special Agent Alderman (App. 14a-15a) to the effect that the subject investigation into the affairs of the taxpayers was allegedly never completed; and this conclusory allegation is supported by averrals that an examination or investigation of the type here involved is complete only when: (1) a formal notice of termination of the investigation has been forwarded to the taxpayers; (2) a report is furnished to the taxpayer wherein he is advised that the examination has resulted in a deficiency and that additional taxes are due; and (3)

the taxpayer is sent a Waiver of Restrictions (Internal Revenue Form 870). The government's reliance upon the statements of Alderman are based on the mistaken belief that the above functions are those performed by a Special Agent in connection with a criminal tax investigation, while, in fact, said functions are solely those of a Revenue Agent and are pertinent only to a civil tax controversy. These procedures, as outlined therein, therefore have absolutely no relevance to the issue presented by the petitioners' application below. It should be further pointed out in reference thereto that the undenied allegations in the reply affidavit of Boris Kostelanetz (App. 16a) unqualifiedly refute the aforesaid statements in the Alderman affidavit on which the government so strongly relies. Said affidavit of Boris Kostelanetz states that the procedures referred to in the affidavit of Special Agent Alderman are not in fact the functions of a Special Agent, nor are they performed in an investigation of the type here involved.

In any event, the allegations of Alderman above referred to at most raise a question of fact which would justify this Court in reversing the decision of the Court below and remanding the matter to the District Court to hold a hearing on a disputed and crucial factual issue, to wit, whether there has been a thrice repeated unnecessary investigation within the statutory prohibition.

2. The government has further, in its responding brief, misconstrued the meaning of the word "unnecessary" in Section 7605(b) so as to base a proposed statutory construction not upon what was clearly intended by Congress to be the meaning of that word, but rather upon what the Internal Revenue Service may administratively feel is a necessary investigation. To permit the Internal Revenue Service to make an *ex parte* determination that an additional investigation is necessary by reason of self claimed inadequacies or deficiencies in their earlier investigations

would be to relegate Section 7605(b) to a mere internal administrative regulation and would clearly circumvent the expressed intent of Congress when it enacted the predecessor thereof.

A rule that would permit the taxing authorities to make repeated investigations upon the theory that, to obtain a complete and thorough investigation, additional work can always be performed, would constitute in essence a modification and repeal by the executive branch of the government (the Internal Revenue Service) of a remedial and protective statute enacted for the protection of the taxpaying citizenry by the legislative branch of the government. Such a rule would violate the principle of statutory construction that the Courts should give force and effect, if possible, to every clause and word of a relevant statute. *United States* v. *Menasche*, 348 U. S. 528 (1954); *F.C.C.* v. *Cohn*, 154 F. Supp. 899, 910 (S.D.N.Y. 1957); *Lafrate* v. *The Liberte*, 106 F. Supp. 619, 621 (S.D.N.Y. 1953); *Queensboro Farming Products* v. *Wickard*, 137 F. 2d 969, 976 (2nd Cir. 1943). The result urged by the government would constitute an abdication by the judiciary of its function of interpretation of the body of law enacted by Congress.

3. The government alleges further in its responding brief that the petitioners had no standing to quash the present summonses and that a taxpayer may move under Section 7605(b) only when he himself is served with a summons and not when the investigation of the taxpayer is in part conducted by summonses served on others as witnesses. Such a result would render the provisions of Section 7605(b) virtually meaningless since every criminal investigation involves third parties as a major source of information. In any event, nothing in the statute or its legislative history warrants so tortured a construction.

The government is further in error in stating that *Martin* v. *Chandis Securities Co.*, 128 F. 2d 731 (9th Cir. 1942),

does not support the precise position here asserted by the petitioners and hence is not in direct conflict with the decision below. The decision in that case necessarily required a holding to the effect that a taxpayer has standing to quash a summons served upon third parties in connection with an investigation of the taxpayer. The decision in *Martin* v. *Chandis Securities Co., supra,* is further reinforced by two other decisions standing precisely for the position here asserted by the petitioners. *Falsone* v. *United States,* 205 F. 2d 734, 742, 743 (5th Cir. 1953); *Arend* v. *DeMasters,* 181 F. Supp. 761 (Ore. 1960).

Foster v. *United States,* 265 F. 2d 183 (2d Cir. 1959), cited by the government, does not deal precisely with the meaning of Section 7605(b) as raised in this proceeding; and, in any event, it merely serves to demonstrate the conflict of decisions between the Second Circuit and the Ninth Circuit on this important issue.

CONCLUSION

The petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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